

NEW INTERPRETATIONS OF CALIFORNIA'S CONTRACTORS' LICENSE LAW

During 1966 three decisions were rendered in California which will noticeably affect the Contractors' License Law found in the Business and Professions Code.¹ One of these decisions, *Latipac, Inc. v. Superior Court*,² has formally acknowledged a substantial, rather than strict, interpretation of section 7031 of the Contractors' Law which requires contractors to be "duly licensed . . . at all times" during performance in order to bring an action for compensation. The other decisions, *Conderback, Inc. v. Standard Oil Co.*³ and *Brunzell Construction Company, Inc. of Nevada v. Barton Development Company*,⁴ have construed section 7026 of this code which defines the term "contractor" in conflicting decisions which indicate a need for legislative clarification.

I

SECTION 7031: STRICT V. SUBSTANTIAL COMPLIANCE

Regulation of the various trades and professions through licensing is today recognized as meeting a public need.⁵ Where a license is required by statute for the protection of the public to prevent improper persons from acting in a particular capacity, absolute failure to license will bar enforcement of the contract.⁶

With this in mind, the California Legislature in 1939 enacted the Contractors' License Law as part of the Business and Professions Code. Section 7031 of that code provides:

No person engaged in the business or acting in the capacity of a contractor, may bring or maintain any action in any court in this State for the collection of compensation for the performance of any act or contract for which a license is required by this chapter without alleging and proving that he was a duly licensed contractor *at all times* during the performance of such act or contract.⁷ [Emphasis added.]

The primary intent of the Legislature in enacting the Contractors' License Law was to protect the health, safety, and general welfare of all persons dealing with those engaged in the contracting business and to afford the public effective and practical protection against incompetent, inexperienced, unlawful and fraudulent acts of building contractors.⁸ However

¹ Contractors' License Law, CAL. BUS. & PROF. CODE §§7000-7145.

² 64 Cal.2d 278, 49 Cal.Rptr. 676 (1966).

³ 239 Cal.App.2d 664, 48 Cal.Rptr. 901 (1966).

⁴ 240 Cal.App.2d 442, 49 Cal.Rptr. 667 (1966).

⁵ *Howard v. State*, 85 Cal.App.2d 361, 193 P.2d 11 (1948).

⁶ See 23 So. CAL. L. REV. 98 (1949).

⁷ CAL. BUS. & PROF. CODE §7031 was added by stat. 1939, §1, ch. 37, p. 384.

⁸ 16 CAL. ADM. CODE 14.

clear the legislative intent may be, it appears that the courts have not always agreed on a proper interpretation of the statutes. Thus, while some California courts have applied section 7031 literally in spite of the equities of the particular case, others have held that absolute compliance with the statutory provisions is not a condition precedent to contractual recovery.

In the 1957 case of *Lewis & Queen v. N. M. Ball Sons*,⁹ often cited as advocating the strict compliance approach to section 7031, the contractor contended that recovery should be allowed on his construction contract even though he had not strictly complied with the licensing statute on the grounds that such a recovery would prevent unjust enrichment. However, this contention was rejected, with Justice Traynor stating:

Section 7031 represents a legislative determination that the importance of deterring unlicensed persons from engaging in the contracting business outweighs any harshness between the parties, and that such deterrence can best be realized by denying violators the right to maintain any action for compensation in the courts of the state.¹⁰

In enforcing a literal interpretation of the statute the court recognized that the Legislature was as much concerned with protecting the public from dishonesty and incompetence in the *administration* of the contracting business as in the actual use of bricks, mortar, and earth-moving equipment.¹¹

In the 1959 case of *Bierman v. Hagstrom Construction Company*¹² a subcontractor was denied recovery for his services when he failed to renew his license for a period of five weeks during the job. Justice Wood distinguished this case from earlier substantial compliance cases by stating, "... in those cases someone had a license at all times during the performance of the work."¹³ One year later in *Steinwinter v. Maxwell*¹⁴ the court again followed the literal compliance approach to deny a partnership recovery. Steinwinter held a valid contractor's license but his partner Bancroft did not. Steinwinter and Bancroft were sole stockholders and president and vice president respectively of another contracting corporation which was duly licensed. Therefore, both individuals had been approved by the licensing board for the issuance of the corporation license. In denying the partnership recovery the court stated:

The application of the substantial compliance rule has been limited to very few cases and we do not feel it should be extended to this case. The partners knew or should have known, that they were required to have a

⁹ 48 Cal.2d 141, 308 P.2d 713 (1957).

¹⁰ *Id.* at 151, 308 P.2d 713, 719.

¹¹ *Id.* at 149-150, 308 P.2d 713, 718.

¹² 176 Cal.App.2d 771, 1 Cal.Rptr. 826 (1959).

¹³ *Id.* at 777, 1 Cal.Rptr. 826, 830.

¹⁴ 183 Cal.App.2d 34, 6 Cal.Rptr. 496 (1960).

contractor's license. They had a valid license in their corporation which they could have used. For reasons unknown they chose not to use it.¹⁵

However, other courts have not been moved to apply the language of section 7031 literally. In *Citizens State Bank v. Gentry*,¹⁶ apparently the first of the substantial compliance cases, a contractor contracted as an individual but allowed his license to expire during performance. He completed the work under the auspices of his corporation which was issued a license in lieu of renewing the individual's license. The court stated:

Where a manifestly unjust and inequitable result would follow a holding that plaintiff contractor was without capacity to sue on his contract, the individual plaintiff in whose name the license stood at the time the contract was made and the corporate entity organized by him in whose name the license stood at the time the cause of action accrued, should be considered as one.¹⁷

In cases following this decision, courts found substantial compliance with section 7031 sufficient when licensed individuals acquired a joint venture license during performance of work with the approval of the other contracting party;¹⁸ when an individual contractor not licensed at the time the contract was executed due to a new classification system became licensed when notified of the new requirement;¹⁹ and when an individual was licensed but the contract was assigned to a corporation formed by the individual with an interval of time lapsing before the corporation was licensed.²⁰

¹⁵ *Id.* at 38, 6 Cal.Rptr. 496, 499.

¹⁶ 20 Cal.App.2d 415, 67 P.2d 364 (1937). While this case was heard before the present statute was enacted in 1939, the present statute is similar to that which was in effect when this case was heard, the only difference being that the earlier statute provided as a penalty for failing to comply with the licensing requirement a fine or imprisonment or both, not to exceed \$500.00 or 6 months.

¹⁷ *Id.* at 420, 67 P.2d 364, 366-367.

¹⁸ *Gatti v. Highland Park Builders, Inc.*, 27 Cal.2d 687, 166 P.2d 265 (1946).

A 1967 decision involving joint venturers, *Proffitt & Durnell Plumbing v. David H. Baer Company* (247 Adv. Cal. App. 596, 55 Cal. Rptr. 764) barred recovery under §§7029 and 7031 of the Business & Professions Code by dismissing an action by a licensed plumbing contractor against a licensed air-conditioning contractor where the former had submitted their combined bid to the prime contractor. The court held plaintiff was not entitled to recover because he had not secured an additional license for acting in the capacity of a joint venturer as required by §7029, and therefore was not "licensed" as required by §7031. The *Proffitt* court relied heavily on *Currie v. Stolowitz* (169 Cal. App. 2d 810, 338 P. 2d 208 (1959)) and *Lewis & Queen v. N. M. Ball Sons* (48 Cal. 2d 141, 308 P. 2d 713 (1957)) which had also denied recovery. Yet, the latter two cases were decided *before* a 1961 amendment was made to §7031 excepting from its provisions "... contractors who are individually licensed under this chapter but who fail to comply with Section 7029." The amended version of this section was not quoted by the court and no effort was made to exclude the *Proffitt* case from its purview.

¹⁹ *Oddo v. Hedde*, 101 Cal. App. 2d 375, 225 P. 2d 929 (1950).

²⁰ *Weiman v. Superior Court*, 51 Cal. 2d 710, 336 P. 2d 489 (1959).

However, not until the 1966 case of *Latipac, Inc. v. Superior Court*²¹ did any court summarize the elements of the substantial compliance doctrine. In this case Justice Tobriner of California's Supreme Court stated the elements necessary to assert the doctrine: (1) that the contractor have a valid license *at time of contracting* [emphasis added]; (2) that he readily secures a renewal of that license; and (3) that the responsibility and competence of the contractor's managing officer are officially confirmed throughout the period of performance of the contract.²²

The facts in *Latipac* which prompted the court's elaboration of the substantial compliance doctrine involved a contracting corporation which was duly licensed when the contract was executed but whose license expired fifteen months after commencement of the work. The contractor continued to perform for ten months and completed the job without renewing the license. In allowing recovery the court stressed that the moment when existence of the license becomes determinative is when the contracting party decides whether the contractor possesses the requisite responsibility and competence and decides whether or not to enter into the relationship. The court stated that "the license, as an official confirmation of the contractor's responsibility and experience, then plays its important role."²³

In view of this decision it would seem in spite of the clear language of section 7031 that contractors must be licensed "at all times" during performance, the California Supreme Court regards it mandatory only that a valid license be held at the time the contract is executed. Since other substantial compliance decisions (on which the *Latipac* court relied) have been on record for many years without legislative action to amend the statute, it would appear that the Legislature has given its approval to a substantial compliance approach where the equities warrant.²⁴ It is submitted that the substantial compliance interpretation of this law as now set forth in the *Latipac* decision reaches the more equitable result in many situations and should be approved by continued acquiescence on the part of the Legislature.

II

SECTION 7026: WHAT IS A CONTRACTOR?

The question confronting the California courts prior to the 1966 case of *Conderback, Inc. v. Standard Oil Co.*²⁵ was whether the factual situation

²¹ 64 Cal.2d 278, 49 Cal.Rptr. 676 (1966).

²² *Id.* at 281-282, 49 Cal.Rptr. 676, 679.

²³ *Id.* at 282, 49 Cal.Rptr. 676, 680.

²⁴ See 10 HASTINGS LAW JOURNAL 89, 91 (1958).

²⁵ 239 Cal.App.2d 664, 48 Cal.Rptr. 901 (1966).

justified application of the substantial compliance doctrine. With the *Conderback* decision, however, a more basic question has now arisen; namely, what is a "California contractor" within the meaning of section 7026 of the Contractors' Licensing Law. This section provides:

The term contractor for the purposes of this chapter is synonymous with the term "builder" and, within the meaning of this chapter, a contractor is any person who undertakes to or offers to undertake to or purports to have the capacity to undertake to or submits a bid to, or does himself or by or through others, construct, alter, repair, add to, subtract from, improve, move, wreck or demolish any building, highway, road parking facility, railroad, excavation or other structures or works in connection therewith. The term contractor includes subcontractor and specialty contractor.²⁶ [Emphasis added.]

The *Conderback* case involved a California corporation, domiciled in San Francisco, which was engaged in the business of building advertising exhibits. From 1960 until it suspended operations in July of 1963 over 300 such exhibits were completed by the Conderback corporation for Standard Oil in California without litigation between the parties. However, the Conderback corporation had never been involved with actual construction work, as defined in section 7026, until July of 1961 when it contracted in San Francisco to construct Standard Oil's building and exhibit at the Seattle World's Fair. During construction of this building in the State of Washington the concept of the exhibit was changed several times by Standard Oil and as a result Conderback lost control of the budget, the design and all coordination between the parties. Upon completion a dispute arose as to payment. Conderback's demands were rejected and litigation resulted with a judgment in favor of Conderback.

On appeal to the District Court of Appeals, Standard Oil's first attack was aimed at the heart of the judgment. It contended that Conderback could not bring or maintain the action (under section 7031) since it was acting in the capacity of a contractor in California (as defined in section 7026) without being duly licensed.

Conderback had no contractor's license whatsoever during the entire time of performance. The State of Washington did not, at that time, have a law requiring licensing of general contractors. Nevertheless, Conderback undertook in California to submit a bid and to administer a substantial portion of the construction work from San Francisco. Certain exhibits were fabricated in San Francisco and then transported to Seattle, and the building itself was designed by an industrial engineer in consultation with a structural engineer and an architect in San Francisco. Conderback would therefore seem to be clearly acting in the capacity of a contractor in California within the meaning of section 7026 of the Business and Professions

²⁶ CAL. BUS. & PROF. CODE §7026 (1963) as amended.

Code. However, the court held that where "a person offers, undertakes or contracts in this state *to construct or demolish a building, project or other improvement located outside of California*, such person does not thereby become one engaged in the business or acting in the capacity of a contractor within this state so as to be subject to the Contractors' License Law."²⁷ [Emphasis added.] Nor did the court feel the fact that the person's principal place of business was located in California necessarily compelled a different conclusion.²⁸

It is to be noted that this court's interpretation of the law was inconsistent with a 1963 Attorney General's opinion on this subject:

Whether a person is engaging in the business or acting in the capacity of a contractor may be determined from the statutory definition of a contractor which is contained in section 7026. . . . Thus a non-resident who mails his bid or otherwise communicates his bid into California for consideration here "submits" his bid within the state. An act of contracting thus takes place within California requiring a California state contractor's license.²⁹

Within one month of the *Conderback* decision a contrary interpretation of the statute, mirroring the 1963 Attorney General's opinion, was adopted in *Brunzell Construction Company, Inc. of Nevada v. Barton Development Company*.³⁰ In *Brunzell*, a Nevada corporation not licensed as a contractor in California was denied damages for anticipatory breach of the contract. The sole shareholder and responsible managing officer of the unlicensed corporation was individually licensed in California as a general contractor and he was also sole shareholder and managing officer of a sister corporation which was a duly licensed California corporation. The facts appeared to leave no question as to the qualifications of the Nevada corporation to act in the capacity of a contractor. The contract was for the construction of an apartment house on land situated in California. Three months after executing the contract and before any actual construction work had commenced the other party sold the property without advising the Nevada corporation. While rejecting the contractor's contention that his right to recovery was not barred under section 7031 because recovery was sought for anticipatory breach rather than performance, the court commented:

It seems to us an overly narrow construction of the code section 7031. Strictly applied, it would lead to the odd rule that one who could not recover for full performance of a contract could nonetheless recover for not performing it at all. *In submitting its bid and executing a contract,*

²⁷ *Conderback, Inc. v. Standard Oil Co.*, 239 Cal.App.2d 664, 679, 48 Cal.Rptr. 901, 912 (1966).

²⁸ *Ibid.*

²⁹ 41 OPS. CAL. ATTY. GEN. 96, 97 (1963).

³⁰ 240 Cal.App.2d 442, 49 Cal.Rptr. 667 (1966).

plaintiff performed acts in the capacity of a contractor. Its action to recover compensation for these acts thus falls within the prescription of section 7031.³¹ [Emphasis added.]

The business of a general contractor may be said to have two interrelated aspects; physical labor at the job site, and administrative paperwork. Each of these activities is a part of the total construction operation. For the most part, the provisions of the Contractors' License Law govern the administrative side of the contracting business, such as licensing, signing and displaying of license, reporting workmen's compensation coverage, license renewals, obtaining construction permits, reporting changes of personnel, etc.³² Not one of the provisions of this Law purports to regulate the manner in which physical labor, such as earth-moving and building, is to be carried out. That aspect of the contractor's job is covered by local building codes.³³ However, the court in *Conderback* appeared to be concerned only with actual construction work and seemingly did not consider the adverse possibilities which could result from inept handling of purely administrative aspects of the job. Yet, litigation in *Conderback* arose not as a result of any difficulties in the actual construction work, but as a direct result of administrative work performed in California—in this instance, financial difficulties caused by the contractor's inability to control the budget. Without proper estimating, planning and other administrative details concerned with construction contracts, the general welfare of contracting parties and all concerned is just as adversely affected as when faulty building practices are employed. Should California allow negotiation, bidding and contracting within the state by unlicensed contractors merely because most of the work is to be performed elsewhere, as was condoned in the *Conderback* case? It would seem that an affirmative answer to this question would be contrary to the decision rendered in *Brunzell*,³⁴ the opinion expressed by California's Attorney General³⁵ and the clear language of section 7026 of the Business and Professions Code.

In comparing *Conderback* and *Brunzell*, it should be noted that neither contractor held a valid license; both contractors "undertook or offered to undertake"³⁶ construction work in California; both "purported to have

³¹ *Id.* at 444, 49 Cal.Rptr. 667, 668-669. It appears noteworthy that the terms of the contract called for \$1,000,000.00 to be paid to the contractor in cash and the remaining \$450,000.00 by promissory notes of the owners. In denying the action on the contract, the court allowed the contractor to amend, stating "the allegations of fraud states a cause of action not barred by the plaintiff's lack of a license."

³² CAL. BUS. & PROF. CODE §§7066-7069; §7075; §7125; §§7140-7145; §7031.5; §7083.

³³ *Latipac, Inc. v. Superior Court*, 64 Cal.2d 278, 291, 49 Cal.Rptr. 676, 686. Mosk, J. dissenting.

³⁴ 240 Cal.App.2d 442, 49 Cal.Rptr. 667 (1966).

³⁵ 41 OPS CAL. ATTY. GEN. 96, 97 (1963).

³⁶ Statutory language of §7026, CAL. BUS. & PROF. CODE.

the capacity”³⁷ to do so; and both “submitted a bid”³⁸ in California in connection with that construction work. Conderback recovered in an action before the District Court of Appeals, First District, Division One, in January of 1966; Brunzell was denied recovery by the District Court of Appeals, First District, Division Three, in February of 1966. In view of these decisions it is apparent that the statute fails to define its own limits; it has proven vague and in need of clarification. Is the intent of the Legislature to regulate the contracting business only when actual construction work is confined to the territorial boundaries of California and to disregard the administrative side of the business when conducted within the State if the construction work itself is performed elsewhere? The statute is silent in this respect. However, it would seem that the thoroughness of this section of the code in its regulation of the administrative details of the construction business indicates that the Legislature intends to reach not only contractors who perform physical work in California but also those who execute their contract in California—even when actual construction work is to be performed elsewhere.

When the Legislature enacts comprehensive regulatory statutes such as those comprising the Contractors’ License Law the courts should not lightly create exceptions to them. In view of the apparently inconsistent interpretations of section 7026 of the statute by two divisions of the District Court of Appeals, it would appear that a clarification defining the limits of this section is needed and would best be accomplished by legislative amendment.

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³⁷ *Ibid.*

³⁸ *Ibid.*